

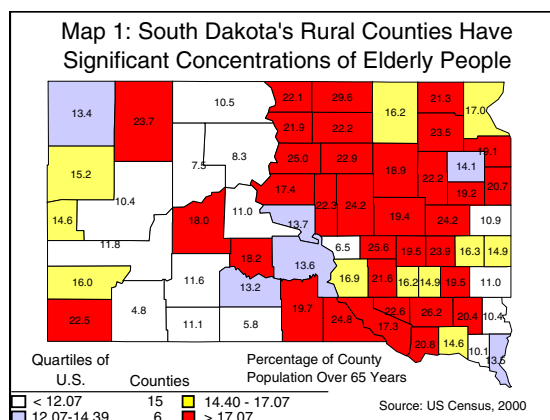
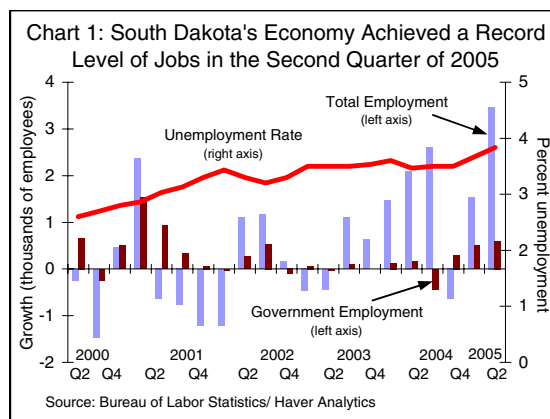
# FDIC State Profile

Fall 2005

## South Dakota

South Dakota's economic expansion gained momentum in the second quarter as employment reached a record level.

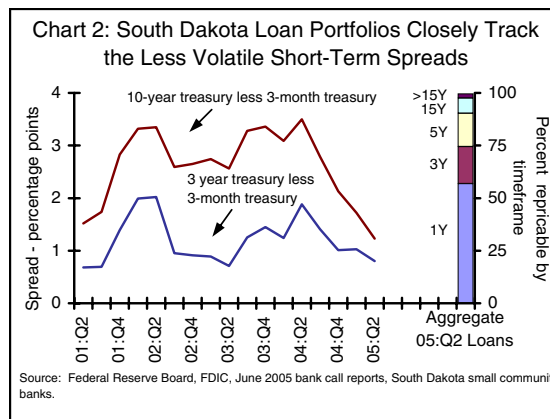
- South Dakota's economy added 3,500 jobs in the second quarter, the largest quarterly increase in six years, to reach a record level of employment (see Chart 1). However, year-over-year employment growth was slightly less than the national rate.
  - South Dakota's government sector, which accounts for more than 19 percent of the state's jobs, avoided the closure of Ellsworth Air Force Base (near **Rapid City**). On August 26, the 2005 Defense Base Realignment and Closure Commission reversed the Department of Defense's recommendation and voted to maintain the base. This was a significant victory for the state, as the base is its second largest employer.
  - The recent hurricanes' effects on the South Dakota economy appear to be modest and are centered on energy. Like other states in the region, energy prices have risen sharply, but supplies have remained adequate. Farmers face substantially higher fuel costs during the harvest season.
- South Dakota's rural counties have relatively large concentrations of elderly people.**
- Based on 2000 Census data, 34 of South Dakota's 66 counties rank in the top quarter of the nation's counties in terms of population older than 65. All but one of these counties are rural (see Map 1).



- Large concentrations of the elderly tend to be associated with rural depopulation, as 33 of the older counties lost population between 1970 and 2000. These counties typically experience the out-migration of younger people seeking educational or employment opportunities.
- The Census Bureau projects that by 2030, 23.1 percent of South Dakota's population will be older than 65, compared with 19.7 percent for the United States.

**Aging populations pose challenges to financial institution funding.**

- Insured institutions operating in rural areas face funding challenges, especially in areas with large elderly



populations. Commonly, when elderly depositors pass away, their deposits quickly move to their heirs' institutions, often located in far-away metropolitan areas.

- Partly resulting from the aging population in South Dakota's rural areas, the state's rural core deposit base has grown just 39.7 percent over the past decade, compared with 52.0 percent for the nation.
- As South Dakota's rural areas continue to grow older over the next few decades, funding may become increasingly difficult to maintain.

### Bank earnings remain solid as rising short-term rates have offset moderate declines in term yield spreads.

- Earnings performance remains positive for most South Dakota institutions. The median return-on-assets ratio was 1.36 percent at June 2005, slightly higher than one year ago. Only 3.3 percent of institutions were unprofitable in the first half of the year.
- The declining spread between three-month and ten-year interest rates has many national banking analysts fretting about potential net interest margin (NIM) compression. However, South Dakota's small community banks do not have the long-term loan exposure that would make them highly responsive to changes in long-term rates<sup>1</sup> Nearly two-thirds of community bank loans reprice within three years; therefore, margins tend to track more closely the much less volatile three-month to three-year treasury spreads (see Chart 2)..
- Given the typical asset-sensitive nature of small community banks, rising short-term rates often benefit small bank margins, even when the yield curve flattens. In fact, the June 2005 median NIM in South Dakota's small community banks was 18 basis points higher than a year earlier.

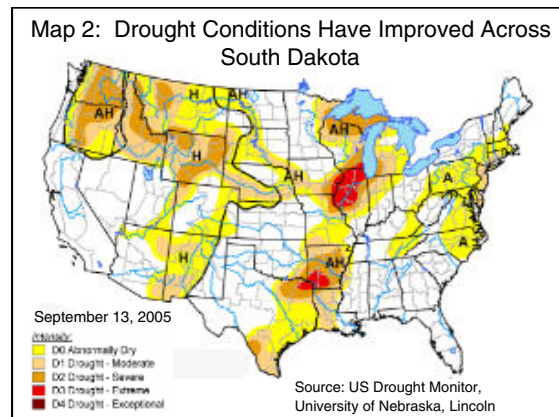
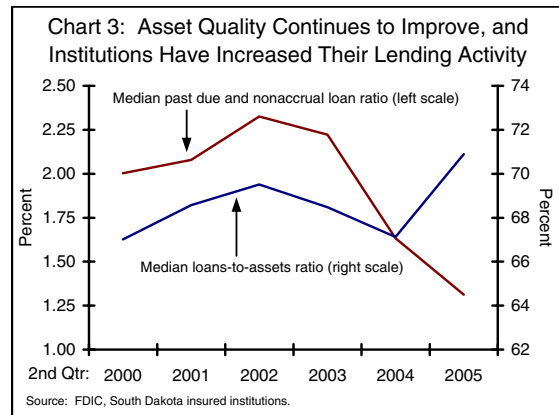
### Asset quality continues to improve at South Dakota's insured institutions, and loan growth is strong.

- Delinquent loans at South Dakota's insured institutions have declined for two straight years, and represented just 1.31 percent of total loans in June 2005 (see Chart 3).
- Although the state has seen a recent spike in consumer bankruptcies as a result of pending bankruptcy reform enactment, the typical South Dakota institution has low consumer loan exposure, and consumer loan charge-offs historically have been minimal. Long-term, bankruptcy reform should be positive for the state's lenders specializing in credit card lending.

- Spurred by business investment, insured institutions are experiencing strong loan growth. Commercial real estate lending was most pronounced growing a median 10.6 percent from a year earlier. Commercial business lending growth was also strong at 7.2 percent.

### Drought conditions have improved across South Dakota.

- Drought conditions have abated across much of the state, with just the western counties experiencing moderate drought (see Map 2).
- The United States Department of Agriculture (USDA) forecasted that South Dakota's 2005 corn crop will be the second largest on record. However, large stocks remaining from last year's harvest should cause lower prices in the upcoming marketing year.
- The soybean crop is forecasted to be larger than normal and reduced yields in the rest of the country and strong demand should lead to higher prices for that crop.



<sup>1</sup>Small community banks are defined as FDIC-insured commercial banks with less than \$250 million in total assets that have been in existence at least three years. At June 30, 2005, these institutions represented 87 percent of all insured institutions in Iowa.

## South Dakota at a Glance

**ECONOMIC INDICATORS** (Change from year ago, unless noted)

| <b>Employment Growth Rates</b>   | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|--|--------------|--------------|--------------|-------------|-------------|
| Total Nonfarm (share of trailing four quarter employment in parentheses) | 1.6%         | 1.8%         | 1.4%         | 1.3%        | 0.2%        |
| Manufacturing (10%)  | 2.2%         | 3.7%         | 3.4%         | 3.3%        | -1.8%       |
| Other (non-manufacturing) Goods-Producing (5%)                           | 6.0%         | 3.9%         | 2.2%         | 1.9%        | 3.5%        |
| Private Service-Producing (65%)  | 1.3%         | 1.8%         | 1.3%         | 1.3%        | 0.2%        |
| Government (19%)   | 0.9%         | 0.7%         | 0.5%         | 0.4%        | 0.5%        |
| Unemployment Rate (% of labor force)                                     | 3.8          | 3.7          | 3.5          | 3.5         | 3.5         |

| <b>Other Indicators</b>   | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|---|--------------|--------------|--------------|-------------|-------------|
| Personal Income   | 4.1%         | 4.9%         | 4.4%         | 6.2%        | 8.8%        |
| Single-Family Home Permits                                      | 3.8%         | -12.0%       | 16.3%        | 15.8%       | 7.7%        |
| Multifamily Building Permits                                    | -5.5%        | -45.3%       | 4.2%         | 57.7%       | 16.1%       |
| Existing Home Sales   | 2.5%         | 8.1%         | 5.8%         | 10.9%       | 4.7%        |
| Home Price Index  | 7.7%         | 7.9%         | 6.9%         | 6.2%        | 4.3%        |
| Bankruptcy Filings per 1000 people (quarterly annualized level) | 4.56         | 3.78         | 3.89         | 3.67        | 3.56        |

**BANKING TRENDS**

| <b>General Information</b>     | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|--------------------------------|--------------|--------------|--------------|-------------|-------------|
| Institutions (#)               | 91           | 91           | 93           | 91          | 94          |
| Total Assets (in millions)     | 433,468      | 436,536      | 437,872      | 442,451     | 85,420      |
| New Institutions (# < 3 years) | 0            | 0            | 0            | 0           | 0           |
| Subchapter S Institutions      | 37           | 37           | 34           | 33          | 32          |

| <b>Asset Quality</b>                                   | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|--|--------------|--------------|--------------|-------------|-------------|
| Past-Due and Nonaccrual Loans / Total Loans (median %) | 1.31         | 1.41         | 1.63         | 1.47        | 1.95        |
| ALLL/Total Loans (median %)                            | 1.50         | 1.61         | 1.67         | 1.62        | 1.75        |
| ALLL/Noncurrent Loans (median multiple)                | 2.91         | 3.04         | 2.27         | 2.69        | 2.11        |
| Net Loan Losses / Total Loans (median %)               | 0.01         | 0.02         | 0.06         | 0.10        | 0.18        |

| <b>Capital / Earnings</b>                    | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|--|--------------|--------------|--------------|-------------|-------------|
| Tier 1 Leverage (median %)                   | 11.06        | 10.75        | 10.96        | 10.56       | 10.72       |
| Return on Assets (median %)                  | 1.45         | 1.30         | 1.39         | 1.32        | 1.15        |
| Pretax Return on Assets (median %)           | 1.89         | 1.74         | 1.72         | 1.65        | 1.57        |
| Net Interest Margin (median %)               | 4.63         | 4.43         | 4.47         | 4.46        | 4.30        |
| Yield on Earning Assets (median %)           | 6.46         | 6.21         | 6.07         | 6.14        | 6.31        |
| Cost of Funding Earning Assets (median %)    | 1.89         | 1.69         | 1.56         | 1.61        | 1.90        |
| Provisions to Avg. Assets (median %)         | 0.00         | 0.00         | 0.04         | 0.08        | 0.09        |
| Noninterest Income to Avg. Assets (median %) | 0.66         | 0.66         | 0.65         | 0.76        | 0.63        |
| Overhead to Avg. Assets (median %)           | 3.14         | 3.23         | 3.09         | 3.24        | 3.18        |

| <b>Liquidity / Sensitivity</b>                         | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|--|--------------|--------------|--------------|-------------|-------------|
| Loans to Assets (median %)                             | 70.9         | 68.9         | 67.1         | 68.4        | 66.7        |
| Noncore Funding to Assets (median %)                   | 17.1         | 15.2         | 14.8         | 15.6        | 13.0        |
| Long-term Assets to Assets (median %, call filers)     | 13.4         | 13.9         | 13.9         | 13.4        | 12.8        |
| Brokered Deposits (number of institutions)             | 27           | 28           | 22           | 25          | 23          |
| Brokered Deposits to Assets (median % for those above) | 3.7          | 3.9          | 3.3          | 3.4         | 3.1         |

| <b>Loan Concentrations (median % of Tier 1 Capital)</b> | <b>Q2-05</b> | <b>Q1-05</b> | <b>Q2-04</b> | <b>2004</b> | <b>2003</b> |
|---|--------------|--------------|--------------|-------------|-------------|
| Commercial and Industrial                               | 89.7         | 87.8         | 94.0         | 84.6        | 82.2        |
| Commercial Real Estate                                  | 56.7         | 57.6         | 42.3         | 55.9        | 41.2        |
| <i>Construction &amp; Development</i>                   | 4.7          | 5.9          | 1.9          | 3.2         | 2.0         |
| <i>Multifamily Residential Real Estate</i>              | 0.0          | 0.1          | 0.0          | 0.0         | 0.0         |
| <i>Nonresidential Real Estate</i>                       | 42.0         | 42.7         | 34.6         | 35.7        | 37.0        |
| Residential Real Estate                                 | 34.8         | 35.5         | 38.8         | 35.8        | 34.6        |
| Consumer  | 43.5         | 43.3         | 46.6         | 50.4        | 50.1        |
| Agriculture   | 219.9        | 220.6        | 233.7        | 230.2       | 242.3       |

**BANKING PROFILE**

| <b>Largest Deposit Markets</b> | <b>Institutions in Market</b> | <b>Deposits (\$ millions)</b> | <b>Asset Distribution</b>    | <b>Institutions</b> |
|--------------------------------|-------------------------------|-------------------------------|------------------------------|---------------------|
| Sioux Falls, SD                | 33                            | 43,738                        | < \$250 million              | 71 (78% )           |
| Sioux City, IA-NE-SD           | 33                            | 2,042                         | \$250 million to \$1 billion | 14 (15.4% )         |
| Rapid City, SD                 | 13                            | 1,457                         | \$1 billion to \$10 billion  | 4 (4.4% )           |
|                                |                               |                               | > \$10 billion               | 2 (2.2% )           |